

Internal Revenue Service
District
Director

Department of the Treasury
1100 Commerce St., Dallas, Texas 75242

Date:

Person to Contact:

Telephone Number:

Refer Reply To:

EO:TS:4920DAEB

Dear Sir or Madam:

We have considered your application for recognition of exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code.

The information presented indicates that you were organized on [REDACTED]. Your Articles of Incorporation state that you are organized exclusively for charitable, religious, educational and scientific purposes, including for such purposes, the making of distributions to organizations that qualify for exemption under Section 501(c)(3) of the Internal Revenue Code.

You state that your organization will be active in the designing, developing and distributing of programs of educational, social, and cultural significance to the public through both the electronic and print media. The educational programs you plan to generate contain such topics as teen pregnancy, gang psychology, rural community problems, illiteracy, and Aids research.

You state your organization should qualify for exemption from Federal income tax for the following reasons:

a) You will distribute your educational programs to affiliate stations to be broadcast to the general public as a supplement to the local commercial stations regular programming.

b) You will charge fees based on a fee structure requiring a radio station to pay only a percentage of a set flat fee represented by the audience composition of the station's local market. (The purpose is to eventually have the poorest radio stations produce programs of the same quality as the richer stations).

c) The future assets of the organization will be distributed in the form of grants to your affiliates, to upgrade the facilities of your affiliates, and to expand your programs and distribution methods to provide a more efficient service.

Section 501(c)(3) of the Code provides exemption for:

"Corporations...organized and operated exclusively for religious, charitable...or educational purposes...no part of the net earnings of which inures to the benefit of any private shareholder or individual..."

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Section 1.501(c)(3)-1(d)(1)(ii) of the Income Tax Regulations provides that all the organizations there described must serve a public rather than a private interest.

Revenue Ruling 72-369, 1972 2 C.B., 245, provides that an organization's providing of a service on a regular basis for a fee is a trade or business ordinarily carried on for a profit. The fact that the services are provided at cost and solely for exempt organizations is not sufficient to characterize the activity as charitable within the meaning of section 501(c)(3) of the Code. Furnishing the services at cost lacks the donative element necessary to establish this activity as charitable.

This Revenue Ruling addresses the fact that your organization will charge a flat fee to your affiliates for the programs you offer. This will be your primary source of income. Even though you state that a fee structure will be implemented for commercial stations whose listening audience is less than that of prominent stations, it still does not satisfy the donative element present in organizations exempt under section 501(c)(3).

This ruling also emphasizes that the fees were charged to exempt organizations and this still did not qualify the organization as exempt. Therefore, when we apply this same concept to your organization which distributes programs for a fee to local commercial stations, it is evident that your organization is not operated exclusively for charitable purposes.

Revenue Ruling 76-4, 1976 1 C.B., 145, provides an example in which an organization formed to produce and distribute free (or at a small cost-defraying amount) educational, cultural, and public interest programs for public viewing via public educational channels qualified for exemption from Federal income taxes under section 501(c)(3). This organization distributed programs only to stations that owned a license from the Federal Communications Commission. This license prohibits these stations from providing any advertising material designed to promote the sale of commercial products or services. Usually, the organization provides its programs to these non commercial and nonprofit stations at no charge. However, in certain circumstances small fees are charged to help defray the production costs of programs. These fees are substantially less than those charged by commercial program production companies. This organization receives most of its financial support from government and foundation grants and contributions from the general public.

This Revenue Ruling clearly illustrates two characteristics lacking from your anticipated operating procedures, that establishes the difference between a commercial business and an exempt organization similar in nature. First, your programs will be distributed to local commercial radio stations that promote commercial product and service advertising. Secondly, you will charge all your affiliates a fee and distribute your programs only to those stations who pay the fee.

The Incorporated Trustees of the Gospel Worker Society v. Comm.; 81-1. USTC, provides an example of some factors deemed to be indicative of an exempt organization operating for a commercial purpose. The following facts were indicative of such a commercial purpose: (1) a substantial accumulation of profits, (2) rapid increases in the salaries of top personnel of the

organization and, (3) the organization's direct competition with commercial publishers.

In analyzing what you have provided we find two of these factors present in your case. You do intend to accumulate a substantial surplus from the fees. You stated that the profits that you accumulate will be used to create grants for your affiliates, upgrade your affiliates facilities, and expand the development and distribution of your own operations. All of these options inure to the benefit of the creators. Secondly, we can only state that the salaries of employees performing services for exempt organizations be reasonable. Regarding the third factor, which is the presence of direct competition with commercial publishers, we need to look no further than your financial data which show gross receipts from sales of merchandise and services at \$[REDACTED] the first year of operations and \$[REDACTED] the second year. However, once all the operating expenses are paid there exists a huge surplus in the amount of \$[REDACTED] the first year that increases to \$[REDACTED] the second year. This clearly establishes that your operations are similar to a commercial business similar in nature.

Based on the activities listed in your application, we have concluded that the operations of your organization do not differ significantly from a commercial business similar in nature. The primary function of the organization is to serve the private interest of its creators rather than a public interest. The activities as taken together present a picture of a distribution business whose primary objectives are profit oriented. Therefore, we conclude that you do not qualify for exemption from Federal income tax under section 501(c)(3) of the Code.

You are required to file, Form 1120, U.S. Corporate Income Tax Returns.

Contributions to your organization are not deductible under section 170 of the Code.

If you do not agree with these conclusions, you may, within 30 days from the date of this letter, file in duplicate a brief of the facts, law, and argument that clearly sets forth your position. If you desire an oral discussion of the issue, please indicate this in your protest. The enclosed Publication 892 gives instructions for filing a protest.

If you do not file a protest with this office within 30 days of the date of this report or letter, this proposed determination will become final.

If you do not protest this proposed determination in a timely manner, it will be considered by the Internal Revenue Code as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Internal Revenue Code provides in part that, "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Court of Claims, or the district court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service."

If this determination letter becomes a final determination, we will notify the appropriate State Officials, as required by section 6104(c) of the Code, that based on the information we have, we are unable to recognize you as an

[REDACTED]

organization of the type described in Code section 501(c)(3).

If you agree with these conclusions or do not wish to file a written protest, please sign and return Form 6018 in the enclosed self-addressed envelope as soon as possible.

If you have any further questions, please contact the person whose name and telephone number are shown at the beginning of this letter.

Sincerely,

[REDACTED]

District Director

Enclosures:
Publication 887
Form 6018